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January 7, 2010

To: Supervisor Gloria Molina, Chair
Supervisor Mark Ridley-Thomas
Supervisor Zev Yaroslavsky
Supervisor Don Knabe
Supervisor Michael D. Antonovich

From: William T Fujioka
Chief Executive Officer

REPORT ON LOS ANGELES TIMES ARTICLE REGARDING HEALTH CARE REFORM (ITEM No. 48-B - AGENDA OF NOVEMBER 17, 2009)

On November 17, 2009, your Board directed the Chief Executive Officer (CEO) to report back regarding a recent Los Angeles Times article about a Centers of Medicare and Medicaid Services (CMS) report that "the proposed national health care reform could be costly to hospitals, nursing homes, and that doctors would turn away Medicare patients, exacerbating existing problems." The CEO was specifically directed to report back on the following:

1. The impact on the Los Angeles County Employees Retirement Association (LACERA) of the proposed drastic cost increase of medical benefits;

2. The impact of the new tax on current employees;

3. The number of seniors in Los Angeles County that would receive reduced benefits based on the CMS report; and

4. Other findings in the CMS report in relation to their impact on County public and private healthcare providers.

The CEO also was directed to report back on any positive impacts which the proposed health care reform may have on the County.

Background Information on CMS Report on H.R. 3962

The Los Angeles Times article, cited by the Board motion, states that a government report finds that proposed Medicare cuts in the House health care reform bill, would reduce benefits for some senior citizens and could jeopardize access to care for millions of others. While the news article cited findings from a "government report," it was based on a memorandum from Richard Foster, the Chief Actuary of the CMS, which estimated the non-tax financial impacts of H.R. 3962, the House-passed health care reform bill, over ten years (2010 through 2019) at the request of House Republicans. This memorandum presented the CMS Actuary's estimates of the net impacts of the bill on federal government and national health expenditures and the number of insured persons. According to the article, the estimates, and other information provided in it "do not represent an official position of the Department of Health and Human Services or the Administration."

The CMS Actuary also stated that "the actual future impacts of H.R. 3962 on health expenditures, insured status, individual decisions, and employer behavior are very uncertain. The legislation would result in numerous changes in the way that health care insurance is provided and paid for in the United States, and the scope and magnitude of these changes are such that few precedents exist for use in estimation." He further cited numerous caveats and assumptions that make the estimates of the bill's impacts very uncertain. For example, he cited how the bill does not specify a definition of income for determining Medicaid eligibility under its proposed Medicaid expansion, making estimates of newly Medicaid eligible persons more uncertain. In addition, he also noted the difficulty of even accurately estimating the number of uninsured persons, let alone the number of uninsured undocumented immigrants who would not be eligible for any of the expanded Medicaid or health coverage and new health insurance subsidies.

Impact on LACERA of the Proposed Cost Increase of Medical Benefits

The health care reform provisions affecting LACERA are those which would help finance health coverage expansions by reducing Medicare expenditures. According to the CMS Actuary's estimates, the House bill would reduce net Medicare spending by $570.6 billion over ten years, including estimated savings of more than $200 billion by reducing payments under Medicare Advantage plans, which are Medicare health plan options offered by private firms under contract with CMS. Medicare Advantage plan options, which include Health Maintenance Organizations (HMOs) and Preferred Provider Organizations (PPOs), are required to provide at least the same scope of benefits as traditional Medicare, but they also generally provide extra benefits, such as vision and dental benefits. Members of LACERA are given the option to participate in Medicare HMOs and other Medicare Advantage options.

When Medicare HMOs and Medicare Advantage plans first were introduced, their reimbursement rates were below average traditional Medicare Fee-For-Service (FFS) costs. However, over time, Congress increased Medicare Advantage payment rates to the point where they currently are significantly higher than prevailing Medicare FFS costs. Under H.R. 3962, Medicare Advantage reimbursement rates would be reduced to those of traditional Medicare FFS costs. LACERA believes that the reduced reimbursement rates would result in a significant increase in Medicare Advantage plan premiums that the County pays as the plan sponsor. According to LACERA, its average Medicare HMO premiums currently range from $190 to $300, 89% of which is paid by the County, as the plan's sponsor. In addition, LACERA indicates that reductions in Medicare reimbursement would increase the level of health expenditures that instead must be financed by the County.

Impact of New Tax on Current Employees

The House-passed health care reform bill (H.R. 3962), which the CMS report analyzed, did not include a new tax which would affect benefits for current County employees. The Senate version, however, would impose a 40% excise tax on "high-cost" employer-sponsored health insurance plans beginning in 2013. The Senate bill specifically would impose a 40% tax on combined employer and employee contributions exceeding a threshold amount of $8,500 for single coverage and $23,000 for family (multi-person) coverage in 2013. The threshold would be increased by $1,350 to $9,850 for single coverage and by $3,000 to $26,000 for family coverage for any employee in a high-risk occupation (e.g., law enforcement officers, firefighters, rescue, and ambulance personnel) and for a retiree over age 55 who is not entitled to benefits or eligible for enrollment under Medicare. For each year after 2013, the threshold amounts would be adjusted for the change in the Consumer Price Index for Urban consumers (CPI-U) plus one percentage point. This new tax would apply to health insurance benefits for retired as well as active (current) employees.

The impact on this new excise tax on the County and its employees will be affected by variables, such as the future number of employees, future health insurance premium cost increases, and the choice of health insurance plans into which employees enroll in the future. While the new tax technically would be imposed on insurance companies, the consensus is that the impact of the tax would be passed through to employees, affecting their compensation. It is expected that the 40% tax on high-cost health insurance plans will discourage employers from offering and/or employees from selecting high-cost plans, and encourage employers to provide their employees with greater compensation in the form of taxable cash in lieu of tax-free health benefits.

Assuming no changes in the County's health insurance plans, number of active County employees enrolled in them, and 10% average annual growth rate for County health insurance premiums, the County's Department of Human Resources estimates that the percentage of active employees receiving health insurance benefits from the County whose health insurance premiums would be subject to the excise tax would grow from only 3% in 2013 to 95% in 2019 and that the total excise taxes paid would grow from $4.18 million in 2013 to $158.49 million in 2019.

The impact of the excise tax on the County will grow significantly over time to the extent that health insurance premium costs grow at a much faster rate than the annual adjustment for the excise tax threshold, which is tied to the CPI-U plus one percentage point. As health premium costs grow relative to the premium thresholds for excise taxes, the premiums for an ever growing number of employees will be subject to the excise tax. The Congressional Budget Office and Joint Committee on Taxation estimates that Federal revenues from the excise tax would grow from $7.1 billion in 2013 to $34.6 billion in 2019, and grow by roughly 10% to 15% in the following decade.

As noted earlier, the 40% excise tax also would apply to employer-sponsored health insurance plans for retired employees. Assuming a 10% annual growth rate in health insurance premiums for retired County employees, LACERA estimates that, in 2013, the health premiums of 30% of all retired employees would be subject to excise taxes totaling $17.66 million in taxes. The percentage of affected retired employees would grow to 45% by 2019 when the tax payments would total $98.87 million.

<u>Number of Seniors Who Would Receive Reduced Benefits Based on the CMS Report</u>

The Board order requests a report back on how many seniors in Los Angeles County would receive reduced benefits based on the CMS report. The number of seniors in the County who would receive reduced benefits based on the CMS report cannot be determined. The CMS Actuary did not state that the House bill "would sharply reduce benefits for some seniors and could jeopardize access to care for millions of others," as reported in the news article. Instead, his memorandum's only statement relating to reduced benefits for senior citizens was a statement that a reduction in Medicare payment rates for Medicare Advantage plans would "result in less generous benefit packages" under such plans because, as explained in a footnote, Medicare Advantage plans use revenues to "reduce Medicare coinsurance requirements, add extra benefits such as vision or dental care, and/or reduce enrollee premiums for Part B or Part D of Medicare." The bill neither directly reduces Medicare benefits nor requires Medicare Advantage plans to reduce their scope of benefits. Optional benefits under individual Medicare Advantage plans only would be affected if the plans were to respond to reduced Medicare reimbursement rates by eliminating optional benefits.

Neither did the CMS Actuary state that the bill "could jeopardize access to care for millions of others." Instead, in the Medicare section of the memorandum, he stated that if Medicare providers do not improve their productivity as expended in the bill's annual productivity adjustments to Medicare payment rates, then "providers for whom Medicare constitutes a substantive portion of their business could find it difficult to remain profitable and might end their participation in the program (possibly jeopardizing access to care for beneficiaries)." He made this statement in the context of explaining why the estimated savings shown in the memorandum for the category of Medicare proposals relating to productivity adjustments may be unrealistic. It is one example of how the CMS Actuary repeatedly emphasized the uncertainty and limitations of his estimates of the financial and coverage impacts of the House health reform bill.

Other Findings in the CMS Report in Relation to Their Impact on County Public and Private Health Care Providers

The Board order also asked for a report back on other "findings in the CMS report in relation to their impact on County public and private health care providers." As noted earlier, the CMS Actuary's memorandum presented the estimated impacts of the House health care reform bill on federal government and national health expenditures and the number of insured persons. It did not specifically address the potential impacts on providers, and generally included statements on such impacts only in relation to how they affect estimates of the financial impacts of the bill.

For example, in a section of the memorandum on the caveats and limitations of the estimates, the CMS Actuary indicated that his estimates assumed that the increased demand for health care services could be met without market disruptions, but that, in practice, "supply constraints might interfere with providing services desired by the additional 34 million insured persons," and went on to discuss how providers might behave in alternative ways, such as by "successfully negotiating higher fees in response to the greater demand" or alternatively by "accepting more patients who have private insurance (with relatively attractive payment rates) and fewer Medicaid patients, exacerbating existing access problems for the latter group." Such statements do not represent "findings" about the potential impacts of the House bill. Instead, they are caveats about the high degree of uncertainty of any estimates of the impacts of the legislation.

Moreover, the CMS Actuary did not prepare any estimates of the impacts of the bill on individual states or local areas, such as the County. This is significant because the bill's provisions would have varying impacts on different state and local governments and providers in different states and counties, including Los Angeles County. For example, Medicaid programs, the number and rate of uninsured persons and characteristics of uninsured persons vary significantly among states and counties. As a result, the impacts of the bill's health coverage provisions -- especially its Medicaid provisions which would have the greatest impact on the County -- also will vary significantly among states and counties. Therefore, the CMS' national estimates of the House bill cannot be used to determine its County level impacts.

Positive Aspects of Proposed Health Care Reform on the County

The Board order finally requested for a report back on any positive aspects of the proposed health care reform on the County. The most positive impacts, by far, of pending health care reform legislation on the County relate to provisions that would extend Medicaid coverage to previously ineligible persons – most notably, medically indigent adults for whom counties in California are responsible for providing medical care under State law. Expanded Medicaid eligibility would benefit the County by increasing our Medicaid revenue and reducing our uncompensated costs. The County also would benefit to the extent that the legislation would make available increased funding for public health and prevention programs and extend 340B prescription drug discounts to inpatient drugs.

This Office will continue to pursue positions on health care reform legislation, which would benefit the County, such as by expanding Medicaid eligibility and opposing provisions which would hurt the County, such as by reducing Medicaid Disproportionate Share Hospital (DSH) funding and imposing an excise tax on health insurance premiums for County employees.

If you have any questions, have your staff contact Ellen Sandt, Deputy Chief Executive Officer at (213) 974-1186 or Ryan Alsop at (213) 974-1100.

WTF:ES
RA:MT:cg

c: Executive Office, Board of Supervisors
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Department of Human Resources
Los Angeles County Employee Retirement Association